MICHAEL J. MURPHY
State Treasurer

Spring 2002

The LOCAL View

Local Option Capital Asset Lending

LOCAL announces new financing schedule

The LOCAL Program Advisory Group, at its March 20 meeting, recommended a new, quarterly issuance schedule for the LOCAL equipment program.

The schedule is designed to meet the needs of local agencies while addressing concerns about "market saturation" raised by the Office of the State Treasurer's Debt Management staff and the program's financial adviser at the advisory group's previous meeting.

Washington State Treasurer Mike Murphy said the new schedule will become effective with the August 2002 issue. (See chart below.) The number of equipment COPs (Certificates of Participation) each year will be reduced from six to four, and cutoff dates will be moved to the first of the month.

The LOCAL Program allows local agencies seeking financing for equipment or real estate to pool their needs to save on the costs of issuance and gain lower interest rates through competitive bidding. LOCAL Program payments can be paid to the vendor directly or as reimbursement to the agency. The new schedule applies only to equipment.

Besides affecting the timing of issuance, the new schedule will result in larger dollar amounts in each issue, which will make the COPs more attractive to underwriters.

Larger issue sizes will generally expand marketability, leading to lower interest rates. Larger issues also allow fixed costs of issuance to be spread over a larger financing base, which reduces financing costs even more for individual LOCAL users.

"Fewer issues will mean we can be more efficient and meet our goal of 'working smarter,' " said Treasurer Murphy. "We'll need less time for database entry, settlements, official statement review, and other issuance activities."

Questions about the new schedule, or anything else about the LOCAL Program, can be directed to LOCAL staff members at the numbers to the left.

New schedule for equipment financings

(Effective August 2002 financing)

Cutoff	Sale date	Funding date	First payment
Feb. 1	First week of March	March 10-15	June 1, year of issue
May 1	Last week of May	June 5-10	Dec. 1, year of issue
Aug. 1	Last week of August	Sept. 5-10	Dec. 1, year of issue
Nov. 1	First week of December	Dec. 10-15	June 1, following year

We moved

Administrative staffers of the Office of the State Treasurer, including LOCAL staff, have moved to a new Tumwater location to accommodate the renovation of the Legislative Building on the Capitol Campus.

Our new address:

3200 Capitol Blvd. S.E.
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Our mailing address and phone numbers stay the same:

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Competitive or negotiated? On Murphy's watch, it's competitive

By **Michael J. Murphy**
Washington State Treasurer

There are arguments for both sides on the question of negotiated bond sales vs. competitive, but I've done only competitive in my five years as State Treasurer. For me, it's the right call, and I believe it can be the best choice for you, too.

When I make decisions that involve millions of dollars, I want the public to know I will always treat every penny of every tax dollar very carefully. When we do a competitive sale, we know we did the best transaction possible, for the issuer and the taxpayer.

Why? Because competitive bond sales work. First of all, stable state and local governments like mine and yours are readily accepted in the bond market. We can attract enough bidders to make a competitive sale worthwhile. Second, you pay less. And third and most important, you are in charge of the transaction, from start to finish, which is control you don't have over a negotiated sale.

I can hear you saying, "Sure, competitive works for a big player like the state of Washington, but I'm too small to make it work for me." You might be hearing exactly that same thing from investment bankers. So who should sell competitively? It might well be you.

Ask yourself these questions: Will I have to settle for an unnecessarily high interest rate if I choose a negotiated sale? What additional finance charges will I pay if I opt for a negotiated sale? The benefits of a competitive sale are clear.

If you are a broad-based, general-purpose borrower and a well known, stable issuer who ventures regularly into the marketplace, you almost certainly will gain from a competitive sale. If your bond rating is 'A' or above and your rating outlook is stable, so much the better.

As far as structuring the debt, pledged revenues such as general obligation or strong revenue bonds are ideal for a competitive sale.

How about the current market? On the selling side, the interest rate environment is great right now. But can you get enough bidders? Let me cite our most recent sale (January 2002) as an example: we got three bidders for a $253 million GO various purpose bond offering and four bidders for $338 million in GO motor vehicle fuel tax bonds.

Every single true interest cost (TIC) bid for the two offerings was under 5 percent. One related note: We do all our bond sales electronically, and I believe that also fosters good competition.

As I said above, one great advantage of a competitive sale is the control you have over the transaction.

- You *time* the offering;
- You open the sale to underwriters to *compete* for your business;
- You pay a *lower spread*;
- You accept the *least costly* bid.

How do you get started toward doing a competitive sale? First, put together your financing team, including bond counsel and an independent financial adviser.

Your bond counsel can do much more for you than render legal opinions, though that is important. Counsel should be able to help you prepare and review documents, help with presentations, prepare or review contracts, and prepare the official transcript.

As long as you're paying them, there are other things bond counsel can do for you: offer tax advice, keep an eye on your compliance and disclosure responsibilities, and help with requests for proposals.

Your financial adviser (FA) is an equally important player in any bond sale. Why hire an FA? You do this so the underwriter is not the only voice you hear, even if you choose a negotiated sale. An independent FA represents its issuer-client – you – and should be thought of as an extension of your staff.

Underwriters, in contrast, can't represent issuers independently for two big reasons: they act on their own account and they also represent the interests of investors.

Your financial adviser can help set up the financial structure of the transaction, prepare the preliminary official statement, prepare the notice of sale and advertise the sale, identify the date of the sale, and prepare bid forms.

Once these professionals are working for you, what might have seemed a daunting task

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Resolutions or ordinances: Which one to use?

by **Jeff Nave**
Foster Pepper & Shefelman

Through December 2001, the State Treasurer's LOCAL Program had provided funds for 35 cities and towns, including some of the largest (and smallest) in the state.

Many of these borrowings financed police and emergency vehicles. However, the LOCAL Program has funded such diverse items as boats, lawnmowers and energy conservation improvements.

There remain similarities between the LOCAL Program and other methods by which cities and towns borrow money. Perhaps the most important is that a city or town must authorize LOCAL Program financing contracts by passing an ***ordinance***.

Why can't cities and towns just adopt resolutions?

The State Treasurer understands that procedures for passing ordinances are more complex than for resolutions. Many city charters and codes require multiple readings of ordinances before passage, a procedure generally not required for resolutions. Likewise, state law requires that most cities publish their ordinances. (For some cities, ordinances do not become effective until published.)

These procedures can seem cumbersome and expensive compared to adopting a resolution. However, they are necessary.

Cities and towns are general-purpose municipal governments (as opposed to school districts, for instance, which are special-purpose local governments). As a matter of general municipal law, an "ordinance" is considered a legislative act, while a "resolution" is considered an expression of opinion or policy about a particular item of business before a city council.

For this reason, most city charters and city codes require that municipal borrowings be authorized by ordinance. Many state laws refer to ordinances as the proper vehicle by which cities and towns approve borrowings.

The success of the LOCAL Program depends on the validity of the financing contracts local governments sign. When purchasing certificates of participation, investors assume the underlying financing contracts are not subject to challenge. Financing contracts signed by cities and towns could be challenged if they are authorized by resolution. To eliminate any such risk, LOCAL requires all city and town financing contracts be authorized by ordinance.

What can a city or town do to plan?

To prevent a financing contract from being rejected by the State Treasurer, the city or town should allow enough time to pass an ordinance before the deadline for the LOCAL funding round in which the city or town is seeking to participate. Leave sufficient time to satisfy any applicable agenda, "reading" or publication requirements. Also note: some cities and towns must pass ordinances at regular meetings.

Form ordinances for the LOCAL Program are provided in the State Treasurer's LOCAL Program Booklet and Forms (see *http://www.wa.gov/tre/local-bookE.pdf*).

As a matter of general municipal law, an "ordinance" is considered a legislative act, while a "resolution" is considered an expression of opinion or policy about a particular item of business before a city council.

Quick fact

The LOCAL Program has financed more than $30 million in equipment and real estate for 131 local governments in Washington.

Notes on pay-as-you-go vs. pay-as-you-use

By **Svein Braseth**
Office of the State Treasurer

One question finance officers often face is whether a project should be paid for using cash or debt: "pay-as-you-go" vs. "pay-as-you-use."

Pay-as-you-go

Under the "pay-as-you-go" approach, capital projects are paid for through the operating budget from available funds for the budget period. The reasons for this approach include mainly: a) lower debt service payments; b) preservation of debt service capacity; and c) future budget flexibility.

However, this approach does not always consider the dollar value of the future benefits of a project. For instance, a new capital project, such as a bridge, road, plant, or station, can provide for additional commercial and residential development, and, as such, increase the tax base. Here, this additional revenue would not be available until the project is built. In other words, under the "pay-as-you-go" approach, no benefits from the project would be received until funds would be sufficient to proceed with the project.

Pay-as-you-use

Under the "pay-as-you-use" approach, capital projects are financed through debt issuance. Some of the arguments for "pay-as-you-use" include a) increased intergenerational utility or equity – meaning that beneficiaries of a project also pay for the project; b) increased project timeliness – projects are built when they are needed (vs. when the funds are available); and c) increased cash-flow stability – by the initial outlay having less of an impact on the funds on

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Competitive vs. negotiated

(from page 2)

to set up a competitive sale is much more manageable.

For me, I can't foresee any circumstances under which I would do a negotiated sale. I just believe selling bonds competitively is the most responsible course for me, as a public servant, and my office.

I know that, over time, many local jurisdictions have become comfortable with negotiated sales. With this article, I hope I've shown you there is a better option.

Pay as you use

(from page 3)

hand and current revenue.

The "pay-as-you-use" approach allows for "maturity matching," where maturities of the debt are matched with the maturities (or the useful life) of the asset being financed. Maturity matching helps assure that equipment or facilities with a short useful life have a correspondingly short maturity schedule and assets with a longer expected useful life have a longer maturity schedule.

Generally, maturity matching has been argued to be "the least risky financing strategy."[1]

1 *Brigham, Eugene F. and Lous C. Gapenski, Intermediate Financial Management, 2nd Edition, pg. 461.*

Important dates: Upcoming LOCAL financings

Real estate			***Equipment***		
Cutoff	**Funding date**	**First payment due**	**Cutoff**	**Funding date**	**First payment due**
August 15, 2002	November 1, 2002	June 1, 2003	May 10, 2002	June 15, 2002	Dec. 1, 2002
			Aug. 1, 2002	Sept. 10, 2002	Dec. 1, 2002
			Nov. 1, 2002	Dec. 15, 2002	June 1, 2003

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